

Internal Revenue Service

Department of the Treasury

Washington, DC 20224

Person to Contact: [REDACTED]

Telephone Number: [REDACTED]

Refer Reply to: [REDACTED]

Date: FEB 21 1995

Employer Identification Number: [REDACTED]

Key District: [REDACTED]

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

You were incorporated on [REDACTED] as an [REDACTED] nonprofit corporation. The articles of incorporation state that your purpose is to advance the knowledge and enjoyment of aquatic life and similar and related activities.

Your main activity is holding monthly meetings which about [REDACTED] people attend. The meeting includes a half-hour educational program (e.g., how to raise various species of fish and aquatic plants, how to create aquariums, reports on fish collecting trips and fish conservation in the world); a bowl show (displays of a different fish species owned by members every month); and certification of baby fish and plants grown by members.

Other activities include publishing a monthly newsletter (how-to articles written by members, coming events, minutes from meetings, abstracts of articles in other aquarium society newsletters); maintaining a fish library (made available at the monthly meetings); sponsoring an annual fish show in a public place (typically a shopping mall, at which fish are displayed and the public is educated); sponsoring an annual [REDACTED] specialty show (like the general fish show in all aspects); sponsoring an annual field trip to an aquarium and fish shops in [REDACTED] (available to members and nonmembers for the same fee to defray bus costs); donating aquariums and aquarium books to schools; and occasionally sponsoring fish-collecting trips to local waterways. The activities include contests and judging, with ribbons and plaques going to the winners.

Some of your activity involves fish auctions, upon which you rely for about [REDACTED]% of your total support. You charge a

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percentage commission or a flat fee to the owner/seller of the fish. Auctions are held at each monthly meeting--the auction encourages members to bring in excess stock and offer fish to other members at typically below-wholesale prices, and you retain █% of the proceeds. An auction is held at the annual fish show--many types of fish not otherwise available are sold, and you take a fee of \$█ per bag of fish. At the █ show, you retain █% of the auction proceeds. In addition, you conduct an annual auction in a public location (the auction is the sole event), and take a fee of \$█ per fish bag. According to your proposed budgets for your █ and █ tax years, about █% of the gross auction proceeds, on average, will go to the fish owner/sellers. All auction activity is conducted by volunteers.

You estimate that "well under █%" of your man-hours is spent on the auctions. However, you indicate that the auctions occupy 15-30 minutes of your monthly meetings, which run 1.5-2 hours, and that the annual auction show requires about half the time as the annual general fish and █ shows (which themselves include auctions).

Your proposed budgets for █ and █ itemize the following sources of revenue:

dues	\$█
sponsors	█
entry fees	█
auction (less seller proceeds)	█
bus trip	█
<u>misc. income</u>	█
total	█

Section 501(c)(3) of the Internal Revenue Code exempts from federal income tax organizations organized and operated exclusively for charitable, educational, or certain other purposes, provided that no part of the organization's net earnings inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(c)(1) of the Income Tax Regulations provides that an organization "operates exclusively" for 501(c)(3) purposes only if it engages primarily in activities that accomplish such purposes. It does not operate exclusively for 501(c)(3) purposes if more than an insubstantial part of its activities does not further such purposes.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for

exempt purposes under Section 501(c)(3) of the Code unless it serves a public rather than a private interest. Thus, an organization must establish that it is not organized or operated for the benefit of private interests, such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled by such private interests.

Rev. Rul. 67-139, 1967-1 C.B. 129, distinguished between a gem and mineral club that qualified under section 501(c)(3) of the Code and one that qualified under section 501(c)(7).

In Situation 1, the 501(c)(3) club was formed to advance the earth sciences by stimulating interest and encouraging study therein. Its membership consisted primarily of amateurs and hobbyists interested in geological, mineralogical, and lapidary activities. The club (1) held monthly lectures at which qualified experts discussed topics pertaining to gems and minerals and gave instruction on lapidary techniques; (2) sponsored field trips to collect and study various kinds of rocks and minerals; (3) issued a bulletin containing educational material pertaining to rocks and minerals; (4) maintained a library of reference materials on geological, mineralogical, and lapidary subjects; (5) assisted the local museum in its display of gems and minerals through specimens provided from members' collections; and (6) annually conducted a show for the general public at which members and nonmembers demonstrated lapidary techniques and displayed collections of gems and minerals. Exhibitors at the show competed for awards based upon the quality, workmanship, and variety of their displays. A "swapping" room was maintained to provide an opportunity for the purchase, sale, and exchange of specimens and materials so that the members and others could complete mineral collections, obtain new specimens, and dispose of lapidary works. A nominal fee was charged for show admission and nonmember displays. The general public was invited to attend all club functions and participate in its programs on substantially the same basis as members. Receipts of the society were from membership dues and from the gem and mineral show. Disbursements were for office and club expenses. No salaries were paid; all services were performed by volunteers. The Service reasoned that the organization was educational.

In Situation 2, the 501(c)(7) club was formed by mineralogy and lapidary enthusiasts to disseminate knowledge of mineralogical and lapidary subjects, to promote their application so that greater pleasure may be derived from these activities, and to promote good fellowship among its members. The club (1) held monthly social meetings during which the members discussed

gem and mineral topics and sold, purchased, or exchanged rock and mineral specimens; (2) issued a bulletin containing news of members' social activities and their rock and mineral collections; and (3) annually conducted a show for the general public at which its members displayed their lapidary techniques and mineral specimens. A nominal admission fee, designed to cover expenses of the show, was charged for admittance to the show. The club's funds were otherwise derived solely from membership dues, fees, and assessments. No part of the net earnings of the organization inured to the benefit of any individual. The Service distinguished the club from the 501(c)(3) club in that it was organized and operated primarily for the benefit, pleasure, or recreation of its members, and its activities were only incidentally educational.

In Rev. Rul. 76-152, 1976-1 C.B. 152, the Service held not exempt under section 501(c)(3) of the Code a nonprofit organization formed by art patrons to promote community understanding of modern art trends whose sole activity was selecting for exhibit, exhibiting, and selling art works of local artists, retaining a commission on sales less than customary commercial charges and not sufficient to cover the cost of operating the gallery. The Service reasoned that a major activity of the organization was serving the private interests of those artists whose works are displayed for sale. Since 90% of all sales proceeds were turned over to the individual artists, such direct benefits were substantial by any measure and not merely incidental to its other purposes and activities.

In Society of Costa Rica Collectors v. Commissioner, T.C.M. 84-648, the court upheld the Service's denial of exemption under section 501(c)(3) of the Code. The organization's purpose was the study and promotion of stamps and related history of Central America. Its main activities were a quarterly publication, a stamp authentication service for members, a philatelic library, and distribution of educational materials to collectors clubs. The publication included bid auctions for stamps owned by members, and the organization retained a 10% commission on all sales. The court reasoned that the mail bid sales activity was substantial (commissions were apparently over half of the organization's support), indistinguishable from commercial public sales (except the latter charged 20% commissions), and served private interests.

In St. Louis Science Fiction Limited v. Commissioner, T.C.M. 85-162, the court upheld the Service's denial of exemption under section 501(c)(3) of the Code. The organization was a science fiction club whose main activity was an annual convention. The

convention involved readings, panel discussions, art show and auction (the organization retained a 15% commission), huckster's room, masquerade party, and gaming room. The court reasoned that social and recreational purposes underlied a substantial part of the organization's activities, and that the huckster's room and art auction provided substantial benefit to private interests.

Although your activities are similar to those described in Situation 1 of Rev. Rul. 67-139 in many respects, you conduct auctions to a much greater extent--in this respect your monthly meetings are more like those described in Situation 2. Although you rely on your auctions for nearly █% of your total support, most of the gross proceeds go to the fish owner/sellers rather than you. In addition to providing a market for their sales of fish, the auctions also benefit your members by providing them markets to purchase fish at below-wholesale prices. Like the organizations in Society of Costa Rica Collectors and St. Louis Science Fiction Limited, your auction activity provides substantial benefit to private interests and indicates a substantial non-exempt purpose.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns.

Contributions to you are not deductible under section 170 of the Code.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If you do not protest this ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgement or decree under this section shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted

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administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and copies will be forwarded to your key district office. Thereafter, any questions about your federal income tax status should be addressed to that office. The appropriate State Officials will be notified of this action in accordance with Code section 6104(c).

When sending additional letters to us with respect to this case, you will expedite their receipt by using the following address:

Internal Revenue Service

[REDACTED]
1111 Constitution Ave, N.W.
Washington, D.C. 20224

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

[REDACTED]

[REDACTED]

Chief, Exempt Organizations
Technical Branch 5

initiator

reviewer

[REDACTED]
2/17/95

[REDACTED]
2/21/95